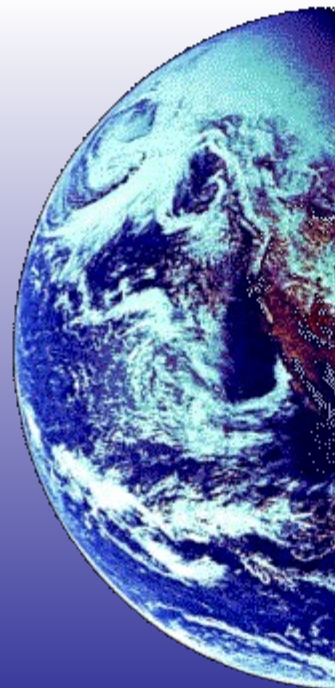




# **Defense Contract Incentives and the Health of the Defense Industry**

**DAEC  
October 7, 2003**

Mr. Terry Marlow  
Vice President  
Government Division

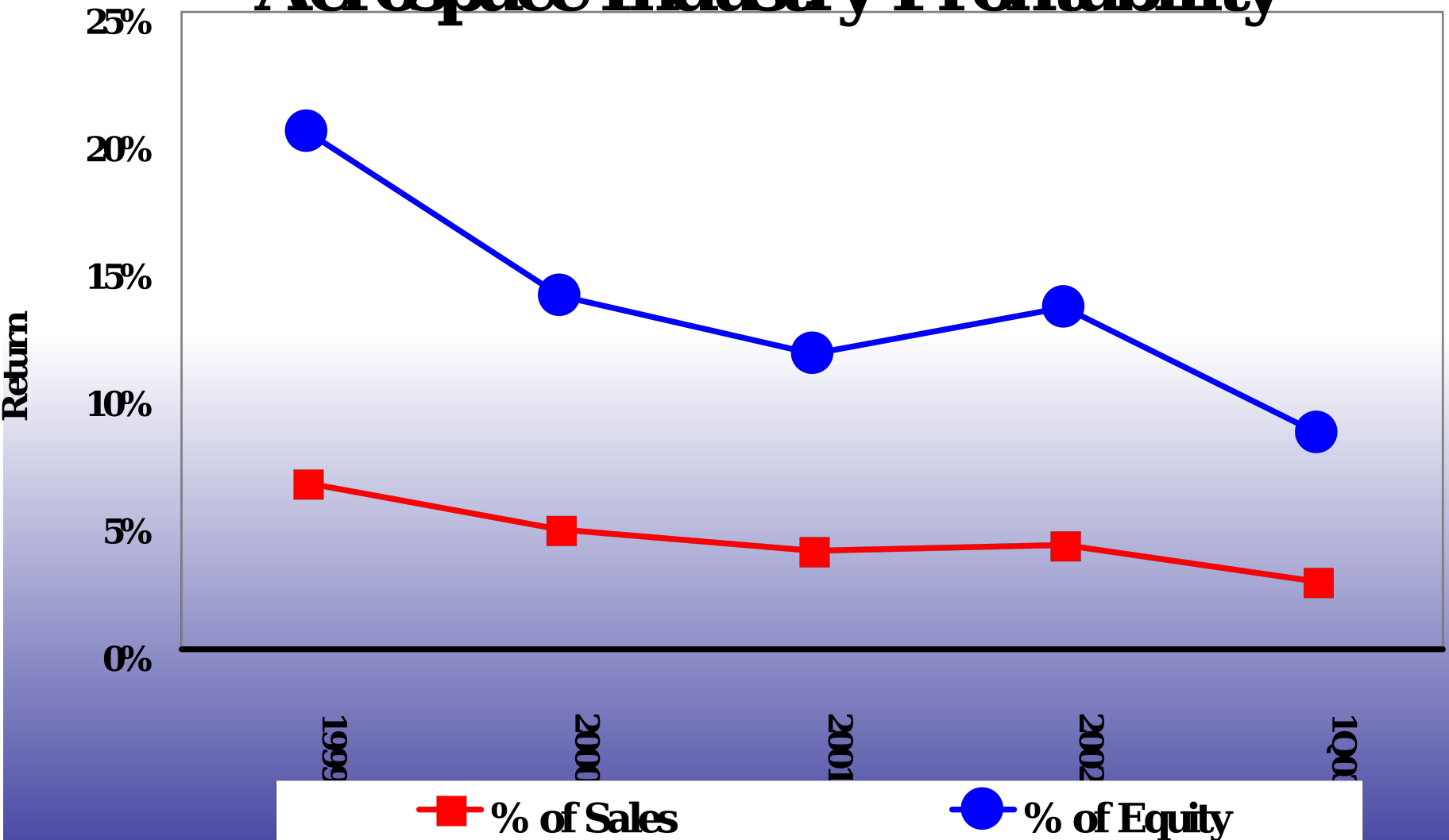




# Industry Concern

- Public statements indicate a perception that program cost and schedule growth results primarily from contractors' failure to manage performance
  - Recently issued profit incentive policies may encourage use of high risk contracts too early in program development
  - Some recent award fee provisions may result in zero fees for minimal cost growth on risky development contracts

# Aerospace Industry Profitability





# Industry Position

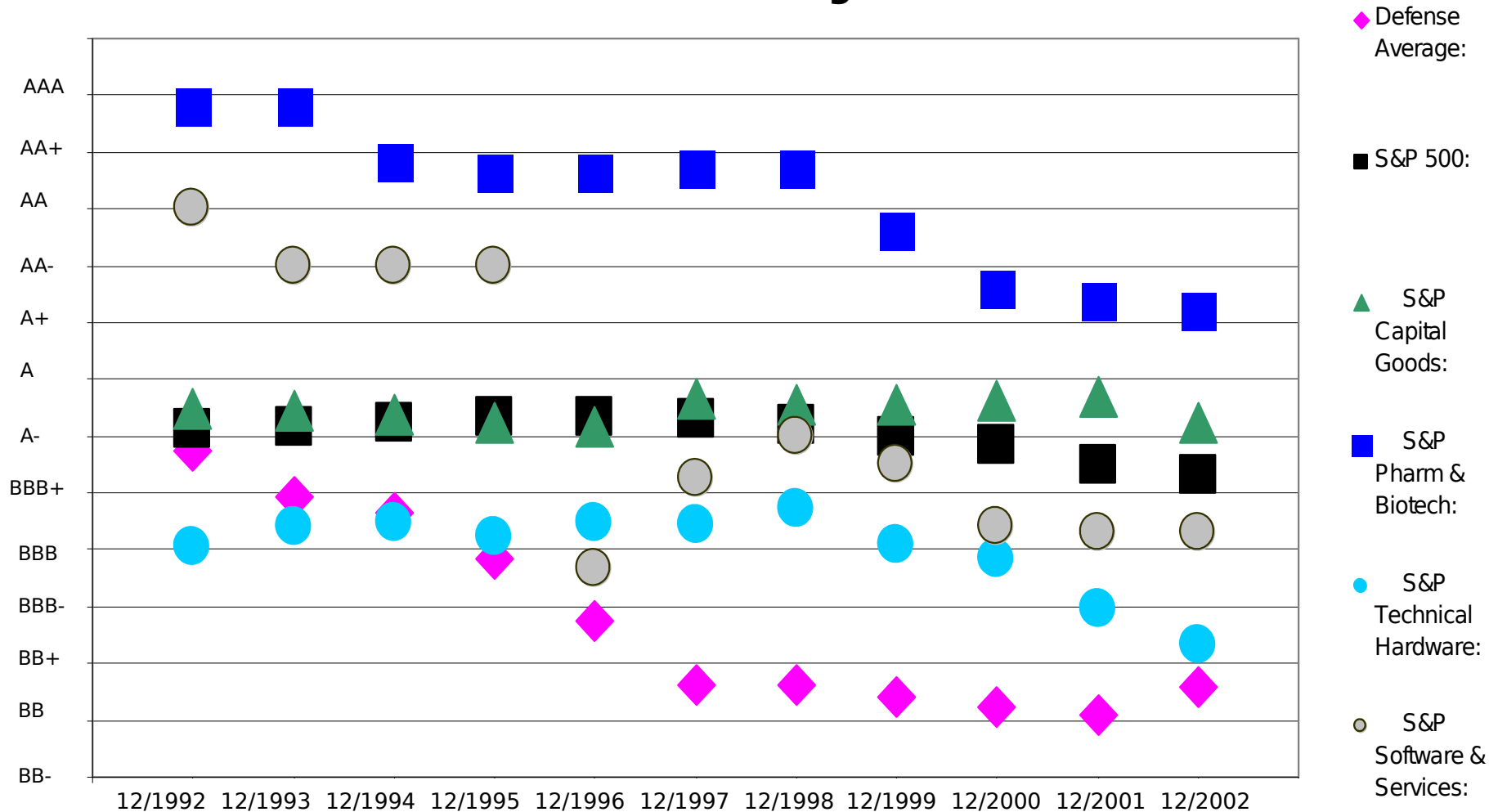
- Industry shares Government's Desire to Minimize Cost and Schedule Growth
  - However, major causes are often beyond contractors' control
    - Requirement changes
    - Unforeseen technical challenges
    - Inadequate budgets
    - Cost estimate optimism in competition



# Current Investment Environment

Defense-Industrial  
Initiatives Group

## Debt Ratings



Source: Factset, S&P  
Compustat, CSIS Analysis



# Industry Proposal

- **Government/Industry Collaboration to Achieve Balance in Services' Profit Policies**
- **Aggressive Use of Draft RFPs to Facilitate Discussion of Appropriate Contract Incentives Prior to Implementation in a Competitive Solicitation**
  - Permit changes to draft RFPs to accommodate industry comments
- **We appreciate Navy and Air Force willingness to work with industry to resolve this matter**

